

ACA TALKING POINTS

FOUR CRITICAL PUBLIC POLICIES TO PROMOTE INNOVATION AND JOB CREATION

Encourage Investments in Qualified Small Businesses.

Congress has long recognized that exempting gains on investments in qualified small businesses encourages investing in innovative start-ups and spurs job formation. Congress approved the 100% capitals gains tax exemption in 2015 in the PATH Act. The last significant overhaul of the US tax system was 1986. Since then most changes have been temporary, implemented by reams of rules. ACA supports a simplified, permanent tax code with the above provisions.

As Congress considers overhauling the tax code, it should:

- **Continue the 100% capital gains exemption**
- **Allow investments in LLCs to count against the 5-year holding period for qualified small business investments if they LLCs convert into C Corps.**
- **Develop clarifications to tax reporting so that investors are more clear that companies are Qualified Small Businesses and meet all requirements.**
- **Increase the time to rollover gains from 60 days to 180 days.**

Expand the Definition of Accredited Investor

The Dodd-Frank Act was enacted in 2010. One of its provisions is that the SEC must review the accredited investor definition every 4 years. The current thresholds are \$200K in income or \$1 million in net worth (excluding the value of a primary residence). Since last year the SEC has been receiving comments about these thresholds. ACA's position is that Congress should:

- **Direct the SEC to maintain the existing financial thresholds.** Some proposals to raise the thresholds to \$450K or \$2.5m net worth would eliminate nearly 60% of eligible households. We must share our voices to refute these. (See enclosed draft letter for members of Congress to submit to the SEC)
- **Direct the SEC to adopt “sophistication” standards that will expand the scope of who is accredited, thus allowing more access to needed funding by small, innovative firms.** Standards might include academic degrees in finance, prior high level fiscal professional experience, or a track record of successful small business investments. Crowdfunding is not a substitute for maintaining the current base of accredited investors

Implement the JOBS Act Properly

Extensive rulemaking by the SEC threatens to undermine Congress's intent to ease the ability of small companies to raise capital. ACA's position is that Congress should:

- **Mandate the SEC to clearly define what constitutes “general solicitation”.** The Act mandated the SEC to allow issuers of private offerings to use general solicitation as long as all purchasers are accredited investors. Issuers must take “reasonable steps to verify” the financial status of purchasers. This is SEC Rule 506(c). Thousands of universities, research organizations, incubators, accelerators, and economic development agencies sponsor events for entrepreneurs to demo products and to meet potential investors, customers and supporters. These activities should be exempted from “general solicitation” so young companies do not inadvertently violate SEC Rule 506(c). ACA's position is that the bi-partisan HALOS Act should be reintroduced and passed by Congress.
- **Direct the SEC to establish more facts and circumstances on how to verify accredited investor status.** The SEC established a “principles based approach” for this verification process and also provided four optional “safe harbors” that require issuers or a 3rd party to review private financial information to verify income and net worth. Angel investors should not be required to reveal private financial data, as is true for crowdfunding participants (Title III) or Regulation A (Title IV) investors. ACA believes membership in an Established Angel Group (EAG) should officially be deemed to meet the verification test. EAG is a high standard that requires adherence to best practices, education and strict codes of conduct. Past SEC clarifications are helpful, but are not clear enough to be accepted by the market. ACA's position is that legislation should be introduced and passed to accomplish this and/or communication with the SEC to provide clarification itself.
- **Direct the SEC to permanently withdraw proposed rule “Amendments to Regulation D, Advanced Form D, and Rule 156.”** The proposed rule came out in 2013 and has never been withdrawn, causing confusion in the startup ecosystem. It would require startups raising money via general solicitation (Rule 506(c)) to file an advanced Form D 15 days before they raise capital, update their business plan information on the same day any changes are made, and provide lengthy disclosures in written materials. This proposed rule allows issuers (entrepreneurs) to make a one-time correction to any violations, but then entrepreneurs would lose their right to raise capital for one year with any additional violations. Given that most startups would have considerable difficulty providing this information every time they change their communications -which

could be daily for many – the rule would put many startups in jeopardy of losing funding and therefore going out of business. Some consumer advocates and the SEC Investor Advisory Committee have recommended that the SEC approve the proposal to be a final rule. ACA’s position is that the rule should be withdrawn by the SEC Commissioners. Congress should communicate to the SEC that the proposal should be withdrawn.

- **Exempt “Demo Days” from the Definition of General Solicitation.** One of the components of the JOBS Act mandated the SEC to allow exempt offerings to use general solicitation as long as all of the people participating in the solicitation event were accredited investors. Decades prior to the JOBS Act and continuing today, thousands of local economic development organizations, universities, incubators, government agencies and research organizations sponsor “demo day” events for entrepreneurs to demonstrate their products and meet potential customers, investors and supporters. This is a nicer version of “Shark Tank.”

ACA believes these demo days should be exempted from the category of general solicitation because they do not involve fraud, are attended by the members of the “startup ecosystem,” and because there are no reasonable steps these entrepreneurs can take to verify that everyone at the “demo day” event meets the definition of an accredited investor. Failure to verify means the young company inadvertently violates SEC Rule 506(c) and could be required to return investment money to their investors. To avoid this situation ACA asked Congress to pass legislation (HALOS Act) to exempt demo days from the category of general solicitation. With bi-partisan sponsorship and support, the House passed our bill (H.R. 79) in January, 2017 with a vote of 344-73. The Senate version (S.588) is pending passage.

Address the “99 Investor Problem.”

Current law restricts the number of individuals who can invest in an angel or venture fund to a maximum of 99 people. Some angel groups and many online platform syndicates pool their money into a fund, or share investment deals between angel groups around the country. The America’s Innovators Act of 2017 (H.R. 1219) would increase the investor threshold to 249 individuals for funds of up to \$10 million. H.R.1219, sponsored by Rep. Patrick McHenry (R-NC), passed the House in April, 2017 with overwhelming bi-partisan support with a vote of 417-3. A similar bill with bi-partisan support in the Senate is S. 444.